

Date 6/1/88

Signature [REDACTED]

MAY ; 2 1988

Dear Applicant:

We have considered your application for recognition of [REDACTED] ation from federal income tax under section 501(c)(3) of the Internal Revenue Code.

Your stated purposes as set out in your Articles of Incorporation are to arrange for the delivery of health care services through independent contracts with physicians, hospitals and other health care providers, to enrollees in, or beneficiaries of, preferred provider health insurance arrangements, health maintenance organizations, and other alternative delivery system arrangements and to engage in other activities which are necessary or beneficial in the delivery of health services under such health insurance arrangements health maintenance organization or other alternative delivery system arrangement.

Your articles provided that the corporation shall have two classes of members designate "Practitioner Members" and Hospital Member. The Practitioner Members shall elect five directors and the Hospital Member shall appoint five directors.

You advise that [REDACTED] and [REDACTED] is a preferred provider organization which arranges for delivery of services to enrollees at discounted rates. You enroll physician members by contracting with them to provide medical services at fixed rates as established by the corporation. You further state that you promote the use of the facilities at [REDACTED] (the hospital member) by contracting with the hospital and the participating physicians to provide services at discounted rates to various member self-funded insurance plans. However, participating physicians are not under exclusive agreements to provide services through [REDACTED]. The physicians may participate in other Preferred Provider Organizations, Health Maintenance Organizations, and other alternative delivery systems.

Each participating physician shall render appropriate services as properly requested under any alternative delivery system you have contracted with and participating physicians will look solely to you for compensation.

Section 501(c)(3) of the Code provides for the exemption from federal income tax of organizations organized and operated exclusively for charitable or educational purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual.

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Section 1.501(c)(3)-1(a) of the Income Tax Regulations provides that an organization must be both organized and operated exclusively for one or more of the purposes specified in section 501(c)(3) of the Code.

Section 1.501(c)(3)-1(b) of the regulations provides that an organization is organized exclusively for exempt purposes only if its articles of organization: (a) limit the purposes to exempt purposes; and (b) do not expressly empower the organization to engage in activities which in the are not in furtherance of exempt purposes.

Section 1.501(c)(3)-1(c)(1) of the regulations provides that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities which accomplish one or more such exempt purposes specified in section 501(c)(3) of the Code. An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Section 1.501(c)(3)-1(d)(ii) of the regulations provides that an organization is not organized or operated exclusively for one or more exempt purpose unless it serves a public rather than a private interest. Thus, to meet the requirements of this subdivision, it is necessary for an organization to establish that it is not organized or operated for the benefit of private interests such as designated individuals, the creators, shareholders of the organization, or persons controlling, directly or indirectly, by such private interests.

Section 1.501(c)(3)-1(e)(1) of the regulations provides that an organization is not exempt under section 501(c)(3) of the Code if its primary purpose and activity is the carrying on of unrelated trade or business as defined in section 513.

Revenue Ruling 54-305, 1954-2 C.B. 127, describes an organization whose primary purpose is the operation and maintenance of a purchasing agency for the benefit of its otherwise unrelated members who are exempt as charitable organizations. The ruling held that the organizations did not qualify under section 101(c) of the Code (predecessor in 501(c)(3)), however, its activities consisted primarily of the purchase of supplies and the performance of other related services. This ruling stated that such activities in themselves cannot be termed charitable, but are ordinary business activities.

Revenue Ruling 69-528, 1969-2 C.B. 127, describes an organization formed to provide investment services on a fee basis only to organizations exempt under section 501(c)(3) of the Code. The organization invested funds received from participating tax-exempt organizations. They were free from the control of the participants and had absolute and uncontrolled discretion over investment policies. The ruling holds that the organization did not qualify under section 501(c)(3) of the Code and stated that providing

investment services on a regular basis for a fee is a trade or business ordinarily carried on for the profit.

Revenue Ruling 75-536, 1975-2 C.B. 127, describes an organization formed to provide investment services on a fee basis only to organizations exempt under section 501(c)(3) of the Code. The organization invested funds received from participating tax-exempt organizations. They were free from the control of the participants and had absolute and uncontrolled did not qualify under section 501(c)(3) of the Code and stated that providing investment services on a regular basis for a fee is a trade or business ordinarily carried on for the profit. The organization is not operated primarily for the promotion of social welfare.

Revenue Ruling 72-369, 1972-2 C.B. 245, describes an organization formed to provide managerial and consulting services at cost to unrelated exempt organizations. The ruling held that the organizations did not qualify for exemption under section 501(c)(3) of the Code. The ruling states that "an organization is not exempt merely because its operations are not conducted for the purposes of producing a profit...providing managerial and consulting services of a regular basis for a fee is a trade or business ordinarily carried on for profit."

In B.S.W. Group, Inc. v. Commissioner, 70 T.C. 353 (1978), the court concluded that an organization whose sole activity consisting of offering consulting services for a fee set at or close to cost to nonprofit, limited resource organizations, does not qualify for exemption under section 501(c)(3) of the Code. The organization entered into consultant-retainer relationships with five or six limited resources groups involved in the fields of health, housing, vocational skills and cooperative management. The organization's financing does not resemble that of the typical section 501(c)(3) organization. They had not solicited, nor received, any voluntary contributions from the public.

In Consumer-Farmer Milk Cooperative, Inc. v. Commissioner of Internal Revenue, 186 F. 2d 68, (1950) the Court denied exemption under the predecessor to section 501(c) of the Code because the organization's purposes is primarily to benefit its members economically and only incidentally to further larger public welfare.

In Better Business Bureau v. U.S., 326 U.S. 279 (1945) the Supreme Court determined that while some activities of the organization under consideration were educational, a substantial purpose of the organization was to promote business, and thus the organization was not operating exclusively for educational purposes.

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In Revenue Ruling 59-545, 1959-2 C.B. 117, the Service recognized as exempt a hospital providing health care to the community because, in doing so, the organization was promoting health.

Your stated purposes, as set out in Article III of your Articles of Incorporation are overly broad and exceed the scope of section 501(c)(3) of the Code. Accordingly, you have failed to demonstrate that you meet the organizational test under section 501(c)(3).

Although some of your activities may contribute indirectly to the achievement of purposes described in section 501(c)(3) of the Code, their overall thrust is to promote business and prevail interest rather than to accomplish exclusively exempt objects.

Your primary activity of providing a pool of physicians to health care plan subscribers and compensating such participating physicians at a negotiated fee is essentially the operation of a billing and collecting Service business with the public in a manner similar to organization which are conducted for profit such as those described in the cases cited above. See sections 1.501(c)(3)-1(e) and 1.501(c)(3)-1(e) of the regulations.

You are essentially a mutual, self-interest type of organization. You negotiate for reduced fees in order to provide direct economic benefit to your subscribers (participating employee members) and sponsoring employers. Any benefit to the larger community is minor and incidental to the economic benefits of your participating employees and employers. Since you are limiting your benefits primarily to subscribing employees and employers and benefitting the community as a whole insubstantially you have failed to demonstrate that you are operated substantially in furtherance of public purposes.

Accordingly, since you are neither organized nor operated exclusively for exempt purposes, you do not qualify for exemption under section 501(c)(3) of the Code. Therefore, you are required to file federal income tax returns. Contributions to you are not deductible to donors under section 170, 2005, 2106, and 2552.

You have the right to protest our ruling in regard to your private foundation status if you believe that it is incorrect. To protest, you should submit a statement of your views, with a full explanation of your reasoning. This statement must be submitted within 30 days of the date of this letter and must be signed by one of your officers. You also have a right to a conference in this office after your statement is submitted. If you want a conference, you must request it when you file your protest statement. If you are to be represented by someone who is not one of your officers, he/she must file a proper power of attorney and otherwise qualify under our Conference and Practice Requirements.

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If you do not protest this proposed ruling in a timely manner, it will be considered by the Internal Revenue Service as a failure to exhaust available administrative remedies. Section 7428(b)(2) of the Code provides, in part, that a declaratory judgment or decree under this section shall not be issued in any proceeding unless the Tax Court, the Claims Court, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted administrative remedies available to it within the Internal Revenue Service.

If you direct further correspondence to us concerning this matter, please include the following symbols on the envelope as part of our address: [REDACTED]. These symbols do not refer to your case by rather to its location.

If we do not hear from you within 30 days, this ruling will become final and copies will be forwarded to your key District Director. Thereafter, if you have any questions about your federal income tax status, including questions concerning reporting requirements, please contact your key District Director.

Sincerely yours,

(signed) [REDACTED]

[REDACTED]
Chief, Exempt Organizations
Rulings Branch

cc: [REDACTED]
[REDACTED]

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Code	Initiator	Reviewer	Reviewer	Reviewer	Reviewer	Reviewer
Surname						
Date	5/3/88	5/12/88				